

AR61



RESOURCES LTD.

1994

ANNUAL

REPORT

PanOil

Corporate Profile

PanOil Resources Ltd. is an independent Canadian Corporation active in exploration, development and production of petroleum and natural gas products in Western Canada. The common shares of PanOil are listed on the Alberta Stock Exchange and trade under the symbol "PRE".

Financial and Operating Highlights

| <i>Financial</i> | <i>1994</i> |
|------------------------|--------------|
| Revenue | \$ 241,436 |
| Public Financing (Net) | \$ 1,156,250 |
| Shareholders' Equity | \$ 2,054,943 |
| Working Capital | \$ 1,150,000 |

| | |
|----------------|------------|
| Shares (Basic) | 10,000,000 |
|----------------|------------|

| <i>Operations</i> | <i>1994</i> |
|----------------------------|-------------|
| Barrels of Oil Per Day | 33 |
| Proven Oil Reserves (bbls) | 25,700 |

Annual Shareholders Meeting

The annual general meeting of shareholders is scheduled for Thursday, May 25, 1995 at 10:00 a.m. at the Calgary Petroleum Club, President's Room, Calgary, Alberta.

Table of Contents

| | |
|---|----|
| President's Message to the Shareholders | 1 |
| Corporate and Operations Summary | 2 |
| Financial Summary | 5 |
| Auditors' Report to the Shareholders | 6 |
| Balance Sheets | 7 |
| Statements of Operations and Deficit | 8 |
| Statements of Changes in Financial Position | 9 |
| Notes to Financial Statements | 10 |
| Corporate Information | 13 |
| Conversion Factors and Abbreviations | 13 |

PRESIDENT'S MESSAGE TO THE SHAREHOLDERS



RESOURCES LTD.

Overview

With the close of the first full year of operations of PanOil Resources on December 31, 1994, I am pleased to report that the company is well positioned, both strategically and financially, to begin creating solid value for its shareholders in 1995.

1994 was a very active year for PanOil, including a corporate acquisition/amalgamation, an initial public offering and participating in the drilling of three wells.

In March, 1994, the company purchased production and undeveloped land holdings by acquiring all the issued and outstanding shares of Gamma Oils Inc. and, on December 31, 1994, the two companies were fully amalgamated.

In October, 1994, PanOil completed the sale of 2,500,000 units, consisting of a share and a warrant, through the facilities of the Alberta Stock Exchange. Net proceeds to the Company, after deduction of agent's commissions, were \$1,156,250.

During the year, PanOil participated in the drilling of three wells in the Paddle River and Red Coulee areas of Alberta, and the Creelman area of Saskatchewan. Of the three wells, in which PanOil had farmed out most of its interests, two were abandoned and one was completed as an oil well. Additional geological studies and acquisition of seismic data are ongoing in the Red Coulee and Creelman areas.

Outlook

PanOil is committed to finding oil or gas reserves and production which will create value for our shareholders. We are working on exploration trends which have reasonable risk exposure, low capital expenditure and significant long term growth opportunities for the Company.

PanOil will focus on several core areas in 1995. At present, the company has a strong liquid capital base, a small inventory of drillable properties and an opportunity to review, and participate in, a stabilizing acquisition market. PanOil evaluated several oil and gas assets for potential acquisition during 1994. We will continue this effort in our search for a property with potential for enhancement.

We thank you for your continued support and look forward to significant additions to reserves and production in 1995.

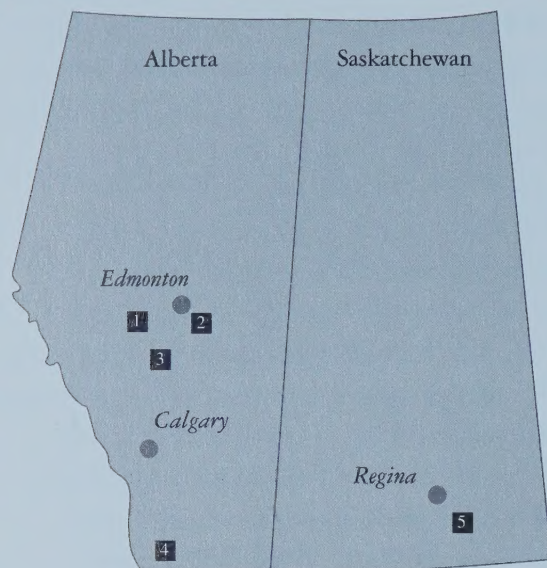
Respectfully yours,

A handwritten signature in dark ink, reading "John B. Maher". The signature is written in a cursive, flowing style.

John B. Maher
President & Chief Executive Officer
March 30, 1995

CORPORATE AND OPERATIONS SUMMARY

Areas of Activity

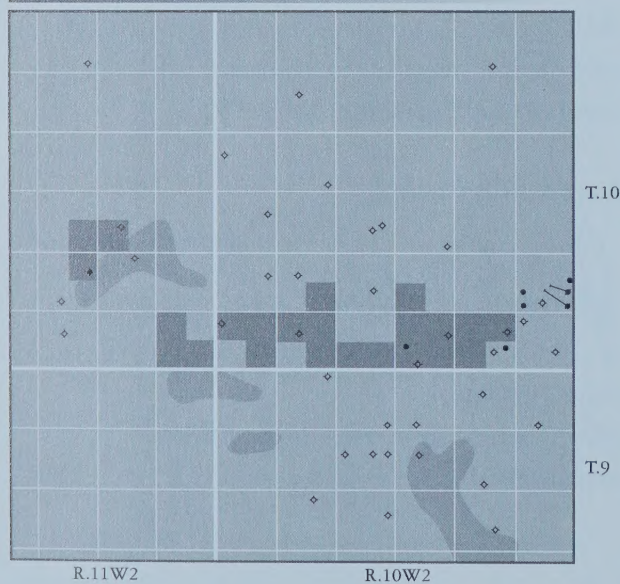


As the oil and gas industry in western Canada shifts from acquisition-led growth to an exploration focus, the quality of the exploration plays in our inventory will be critical to our future success.

PanOil's areas of activity are as follows:

- 1 Paddle River, Alberta
- 2 Woodbend, Alberta
- 3 Spruceview, Alberta
- 4 Red Coulee, Alberta
- 5 Creelman, Saskatchewan

Creelman



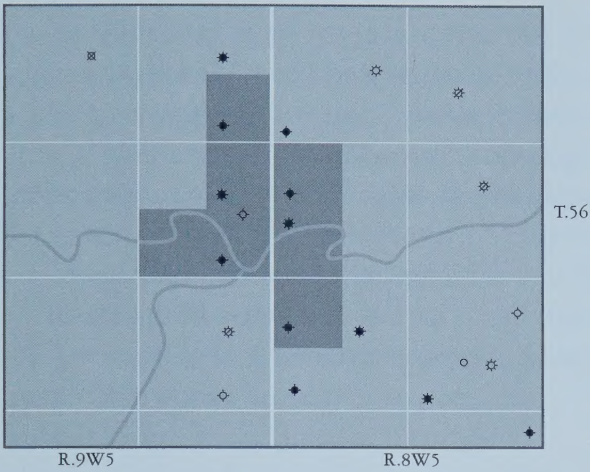
Review of Prospect Areas

Creelman, Saskatchewan

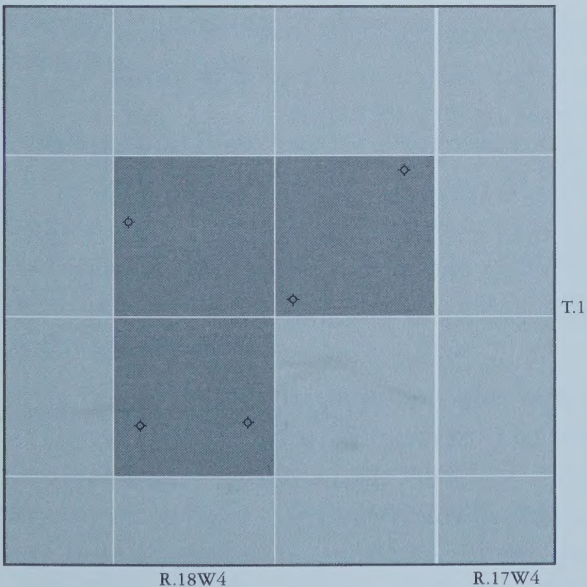
The Creelman area is located in southeastern Saskatchewan, approximately 120 km southeast of Regina. During 1994, PanOil acquired working interests ranging from 12.5% to 30% in (5.75) sections of petroleum and natural gas rights in the area.

In October, PanOil participated in drilling a test well at 5-3-10-10 W2M. The well is currently undergoing production testing.

PanOil and partners plan to complete a new seismic program in the area and will conduct additional drilling in 1995.

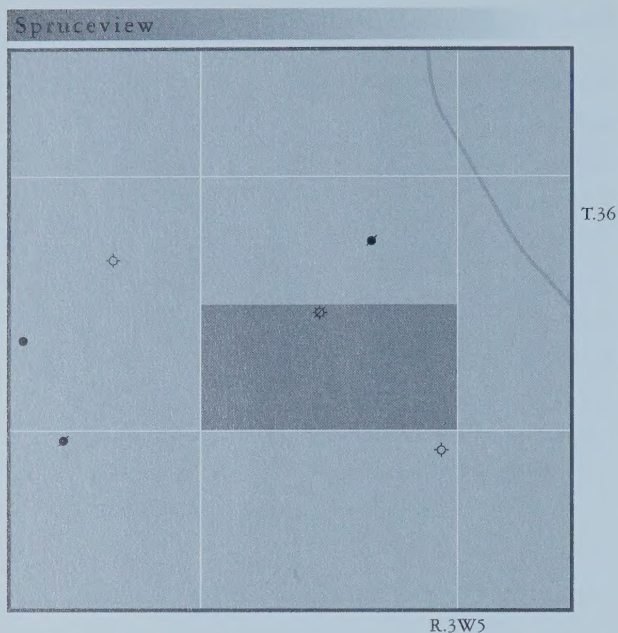
Paddle River

Paddle River, Alberta

PanOil acquired the Paddle River property, approximately 130 km west of Edmonton, from Force Resources Ltd., a predecessor company. A farmout well was drilled in 1994 but was abandoned. PanOil has declined to participate in a second well which was proposed for the property, and the status of the property is now under review pending drilling results by other companies in the area.

Red Coulee

Red Coulee, Alberta

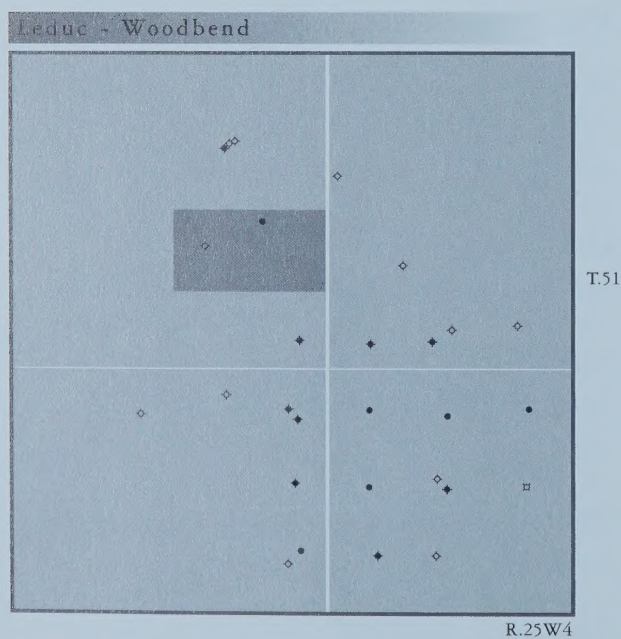
PanOil participated in a seismic program with an option to drill up to five wells to earn an interest in 9,760 acres (1,192 net), approximately 85 km southwest of Lethbridge, in the Red Coulee area of southern Alberta. The corporation was carried through the seismic program and participated in the first test well for 20% to earn 1,920 acres (192 net) in the first block after payout.

The first well encountered a non-reservoir sequence in the Lower Cretaceous target interval and was abandoned. Further studies are underway to select a second exploration location.



Spruceview, Alberta

The 320-acre property, approximately 40 km southwest of Red Deer, which was acquired in the Gamma Oils Inc. acquisition, includes one suspended potential gas well. The well is cased and a completion attempt will be carried out when a satisfactory gas market has been obtained. The pay thickness in the Basal Quartz zone is estimated at 9 metres.



Woodbend, Alberta

Through the acquisition of Gamma Oils Inc., PanOil acquired a 39% working interest in 80 acres of land and one producing oil well at Woodbend, Alberta, on the southwest outskirts of Edmonton. The well averaged 90 barrels of oil per day (33 BOPD net) during 1994. No further development is planned.

At year end the company had received an offer to purchase the property and, as of March 10, 1995, the company had closed the sale of the property.

Exchange Offering Prospectus

On September 26, 1994, pursuant to an Agency Agreement dated August 12, 1994, with Yorkton Securities Inc., the company closed its initial public offering. A total of 2,500,000 units were sold at \$0.50 per unit, for total proceeds (net of agent's commissions) of \$1,156,250.00.

On December 31, 1994, the company had 10,000,000 common shares issued and outstanding. An additional 2,600,000 common shares have been reserved for issue pursuant to the exercise of options and share purchase warrants.

Financial

Revenues - In 1994, with the acquisition and amalgamation of Gamma Oils Inc., the company had operating revenues of \$243,021 consisting of oil sales from its Woodbend property.

Interest and Other Income - Miscellaneous income earned during the year was \$10,593 from both investment of the company's working capital raised by the initial public offering of shares and from the sale of some of Gamma's assets.

General and Administrative

General and administrative expenses amounted to \$199,902 in 1994, excluding one-time costs for the public financing, and engineering and geological costs to evaluate potential oil and gas acquisitions.

Net Loss from Operations - The loss from continuing operations was \$403,457, which was attributable to start-up costs, one-time

financing costs, and a significant writedown of the Paddle River property.

Outlook

Budgeted capital expenditures in 1995 for land acquisition, exploration and development are currently estimated at \$900,000. General and administrative expenses for 1995 have been budgeted at \$300,000. This amount includes adding professional staff to augment exploration and development activities. Potential acquisitions could require considering various financing alternatives, including the use of cash flow, assumption of bank debt or sale of additional equity.

Capital Resources

After amalgamating and rationalizing the bulk of the Gamma Oil assets, PanOil will have in late spring approximately \$1.3 million cash, \$1,127,418 in tax pools, no bank debt and overhead costs of approximately \$25,000 per month.

Capital Expenditures

PanOil incurred the following capital expenditures in 1994:

Petroleum and Natural Gas property and equipment:

| | |
|-----------------------|--------------|
| Property Acquisitions | \$ 931,299 |
| G & G and Seismic | 110,521 |
| Drilling Costs | 55,985 |
| Subtotal | \$ 1,097,005 |
| Furniture | |
| & Equipment (note 4) | \$ 4,478 |
| Total | \$ 1,102,283 |

AUDITORS' REPORT TO SHAREHOLDERS

We have audited the balance sheets of Panoil Resources Ltd. as at December 31, 1994 and 1993 and the statements of operations and deficit and changes in financial position for the periods then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the company as at December 31, 1994 and 1993 and the results of its operations and the changes in its financial position for the periods then ended in accordance with generally accepted accounting principles.

KPMG Perit Marvill Thorne

Chartered Accountants
Calgary, Canada
March 24, 1995

BALANCE SHEETS



RESOURCES LTD.

December 31, 1994 and 1993

| | 1994 | 1993 |
|---|-------------|------------|
| Assets | | |
| Current assets: | | |
| Cash and short-term deposits | \$1,149,208 | \$ 486,382 |
| Accounts receivable | 142,908 | — |
| Share subscriptions receivable (note 6) | — | 50,000 |
| Note receivable (note 3) | 202,000 | — |
| | 1,494,116 | 536,382 |
| Capital assets (notes 4 and 8) | 809,456 | 65,301 |
| Deferred costs | — | 40,467 |
| | \$2,303,572 | \$ 642,150 |
| Liabilities and Shareholders' Equity | | |
| Current liabilities: | | |
| Accounts payable and accrued liabilities | \$ 36,629 | \$ 40,000 |
| Bank loan | 202,000 | — |
| | 238,629 | 40,000 |
| Provision for site restoration costs | 10,000 | — |
| Shareholders' equity: | | |
| Share capital (note 6) | 2,458,400 | 562,150 |
| Warrant subscriptions received | — | 40,000 |
| Deficit | (403,457) | — |
| | 2,054,943 | 602,150 |
| | \$2,303,572 | \$ 642,150 |

Approved by the Board of Directors

Director

Director

See accompanying notes to financial statements.

STATEMENTS OF OPERATIONS AND DEFICIT

Year ended December 31, 1994 and period from incorporation on April 21, 1993
to December 31, 1993

| | 1994 | 1993 |
|--|--------------|------|
| <i>Revenue:</i> | | |
| Petroleum | \$ 243,021 | \$ — |
| Royalties, net of Alberta Royalty Tax Credit | (12,178) | — |
| Interest and other income | 10,593 | — |
| | 241,436 | — |
| <i>Expenses:</i> | | |
| Production | 23,217 | — |
| Depletion, depreciation and amortization | 421,774 | — |
| General and administrative | 199,902 | — |
| | 644,893 | — |
| Net loss for the period, and deficit | \$ (403,457) | \$ — |
| Net loss per share | \$ (0.08) | \$ — |

See accompanying notes to financial statements.

STATEMENTS OF CHANGES IN FINANCIAL POSITION



RESOURCES ♦ LTD.

Year ended December 31, 1994 and period from incorporation on April 21, 1993
to December 31, 1993

| | 1994 | 1993 |
|--|--------------|------------|
| Cash provided by (used in): | | |
| <i>Operations:</i> | | |
| Net loss for the period | \$ (403,457) | \$ — |
| Items not involving cash: | | |
| Depletion, depreciation and amortization | 421,774 | — |
| Funds from operations | 18,317 | — |
| Changes in non-cash working capital | (106,279) | — |
| | (87,962) | — |
| <i>Financing:</i> | | |
| Issue of common shares | 1,856,250 | 602,150 |
| Share subscriptions receivable | 50,000 | (50,000) |
| Change in non-cash working capital | (40,000) | 40,000 |
| | 1,866,250 | 592,150 |
| <i>Investing:</i> | | |
| Acquisition of Gamma Oils Inc. (note 2) | (650,000) | — |
| Capital expenditures | (452,283) | (65,301) |
| Deferred costs | (13,179) | (40,467) |
| | (1,115,462) | (105,768) |
| Increase in cash | 662,826 | 486,382 |
| Cash, beginning of period | 486,382 | — |
| Cash, end of period | \$1,149,208 | \$ 486,382 |

See accompanying notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

Year ended December 31, 1994 and period from incorporation on April 21, 1993
to December 31, 1993

1. Significant accounting policies:

The accompanying financial statements are prepared in accordance with accounting principles generally accepted in Canada.

(a) Incorporation:

PanOil Resources Ltd. (the "Company") was incorporated as Force Resources Inc. on April 21, 1993 by Certificate of Incorporation issued pursuant to the provisions of the Alberta Business Corporations Act. The name of the Company was changed to PanOil Resources Ltd. by Certificate of Amendment dated December 13, 1993.

(b) Petroleum and natural gas operations:

The Company follows the full cost method of accounting whereby all costs associated with the exploration for and development of petroleum and natural gas reserves are capitalized. Such costs include land acquisition costs, geological and geophysical costs, lease rental costs on non-producing properties, costs of both productive and unproductive drilling, production equipment and overhead charges directly related to these activities, net of government grants. Gains or losses are not recognized upon disposition of petroleum and natural gas properties unless crediting the proceeds against accumulated costs would result in a change in the rate of depletion of 20 percent or more.

Accumulated costs, less the costs of acquisition of unproved properties, are depleted and depreciated using the unit-of-production method based on total proved reserves after royalties. Furniture and equipment are depreciated on a straight-line basis over the estimated useful lives of the assets.

The costs of acquiring and evaluating unproved properties are initially excluded from depletion calculations. These properties are assessed periodically to ascertain whether impairment has occurred. When proven reserves are assigned or the property is considered to be impaired, the cost of the property or the amount of impairment is added to the costs subject to depletion.

The net carrying cost of the Company's petroleum and natural gas properties is limited to an estimated recoverable amount being the aggregate of future net revenues from proved reserves, less future site restoration and capital costs, the costs of undeveloped properties net of allowances, future general and administrative costs, financing costs and income taxes. Future net revenues are calculated using prices and costs in effect at the year end without escalation or discounting. Write downs of petroleum and natural gas properties as a result of applying this cost recovery test are classified as depletion, depreciation and amortization.

(c) Joint ventures:

Substantially all of the exploration, development and production activities of the Company are conducted jointly with others. These financial statements reflect only the Company's proportionate interest in such activities.

(d) Provision for site restoration costs:

Estimated future site restoration costs are provided for using the unit-of-production method. Costs are estimated by the Company based on current regulations, costs, technology and industry standards. The annual charge is included in the provision for depletion and depreciation. Actual site restoration costs will be charged to the accumulated provision account as incurred.

(e) Per share information:

Loss per common share for 1994 are calculated using 5,258,333 common shares, being the weighted average number of common shares outstanding.

(f) Deferred costs:

Costs incurred by the Company during 1993 have been capitalized. These costs have been expensed upon commencement of active operations.

2. *Acquisition of Gamma Oils Inc.:*

Effective March 31, 1994 the Company acquired all of the outstanding shares of Gamma Oils Inc. ("Gamma") for a total consideration of \$650,000. The Company and Gamma were amalgamated during 1994.

The acquisition has been accounted for using the purchase method, with the results of operations included in these financial statements from the date of acquisition. The purchase price has been allocated to capital assets.

3. *Note receivable:*

The note receivable is due on demand, and is secured by personal and corporate guarantees from a director and affiliated company. Subsequent to year end the note receivable was collected in full.

4. *Capital assets:*

| | 1994 | 1993 |
|--|--------------|-----------|
| Petroleum and natural gas properties | \$ 1,159,945 | \$ 62,140 |
| Furniture and equipment | 7,639 | 3,161 |
| | 1,167,584 | 65,301 |
| Accumulated depletion and depreciation | (358,128) | — |
| | \$ 809,456 | \$ 65,301 |

At December 31, 1994 the costs of unproved properties not subject to depletion are \$343,344.

5. *Bank loan:*

The bank loan is secured by certain oil and gas properties and personal and corporate guarantees from a director and affiliated company. Subsequent to year end, the principal amount of the bank loan was repaid.

6. *Share capital:*

(a) Authorized:

An unlimited number of common voting shares without nominal or par value

An unlimited number of preferred shares, issuable in series.

(b) Issued and approved for issuance:

| | Common Shares | | Special Warrants | |
|--|---------------|--------------|------------------|-----------|
| | Number | Amount | Number | Amount |
| Issued for cash | 2,750,000 | \$ 155,000 | — | \$ — |
| Issue of Special Warrants net of issue cost of \$52,850 | | | 2,300,000 | 407,150 |
| Balance, December 31, 1993(1) | 2,750,000 | 155,000 | 2,300,000 | 407,150 |
| Issued for cash, net of share issue costs of \$138,750 | 2,500,000 | 1,111,250 | — | — |
| Issued pursuant to acquisition of Gamma Oils Inc. | 1,100,000 | 550,000 | 500,000 | 100,000 |
| Issue of Special Warrants | — | — | 200,000 | 40,000 |
| Conversion of Special warrants into common shares | 3,000,000 | 547,150 | (3,000,000) | (547,150) |
| Issued in exchange for capital assets | 500,000 | 50,000 | — | — |
| Issued in exchange for promotional services | 150,000 | 45,000 | — | — |
| Balance, December 31, 1994 | 10,000,000 | \$ 2,458,400 | — | \$ — |

6. *Share capital (continued):*

- (1) At December 31, 1993, \$50,000 was receivable in respect of the common share and special warrants issues. During 1994, these amounts were received in full.

At December 31, 1994 1,809,219 common shares issued are held in escrow and may not be released from escrow and traded without the written consent of the Alberta Securities Commission Agency and the Alberta Stock Exchange.

(c) *Incentive stock option plan:*

At December 31, 1994, there were 850,000 outstanding options granted to officers, directors and employees of the Company at an exercise price of \$.50. These options expire on various dates to 1999.

(d) *Options:*

The Company has granted options to purchase 500,000 common shares to Yorkton Securities Inc. Each option entitles the holder to purchase one common share for \$0.50, with the options expiring on October 18, 1995.

(e) *Warrants:*

Pursuant to the initial public offering dated September 26, 1994, 2,500,000 warrants were issued. Two warrants entitle the holder thereof to acquire one common share of the Company at a price of \$0.75 per share. No value has been assigned to these warrants by the Company. The warrants are scheduled to expire on April 18, 1995, however application has been made to the ASE to extend the expiry date to October 18, 1995.

7. *Related party transactions:*

The Company participates with certain officers, directors and employees in joint venture operations under the same terms and conditions as those available to third parties.

8. *Subsequent event:*

Subsequent to December 31, 1994, the Company sold certain oil and gas properties for a cash consideration of \$471,000.

Directors and Officers

Garth M. Farr
Chairman of the Board and Director
Calgary, Alberta

John B. Maher
President, CEO and Director
Calgary, Alberta

Alberta E. Chase*
Private Investor
Calgary, Alberta

Wayne R. Sharp*
President, Ramarro Resources Inc.
Calgary, Alberta

W.J.E. (Bud) Shepherdson
Lawyer
Calgary, Alberta

Henry L. Beardsley
Private Investor
Clermont, Florida

* Audit Committee member

Auditors

KPMG Peat Marwick Thorne
Calgary, Alberta

Legal Counsel

Burnet, Duckworth & Palmer
Calgary, Alberta

Banking

Canadian Imperial Bank of Commerce
Calgary, Alberta

Registrar

The R-M Trust Company
Calgary, Alberta

Stock Exchange Listing

Alberta Stock Exchange
Symbol PRE

Shareholder/Investor Inquiries, please contact:

John B. Maher or Garth Farr
(403) 265-8555

Head Office Address:

Suite 1111, Home Oil Tower
324 - 8 Avenue S.W.
Calgary, Alberta, Canada T2P 2Z2

Conversion Factors

To conform with common usage, Imperial units of measurement are used in this report to describe exploration and production. Dollars are Canadian unless otherwise stated.

| | | |
|-----------------------------|---|-----------------------|
| 1 cubic metre (liquids) | = | 6.29 barrels |
| 1 cubic metre (natural gas) | = | 35.31 cubic feet |
| 1 litre | = | 0.22 Imperial gallons |
| 1 hectare | = | 2.47 acres |
| 1 tonne | = | 0.98 ton (long) |

Abbreviations

| | |
|--------|----------------------------|
| bbls | barrels |
| BOE | barrels of oil equivalent |
| BOPD | barrels of oil per day |
| mbl/d | thousand barrels per day |
| mbls | thousand barrels |
| mcf | thousand cubic feet |
| mmbls | million barrels |
| mmcf/d | million cubic feet per day |

PanOil Resources Ltd.
Suite 1111, Home Oil Tower
324 - 8 Avenue S.W.
Calgary, Alberta, Canada T2P 2Z2
Phone: (403) 265-8555
Facsimile: (403) 266-0259

Printed in Canada